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No. 95-1542

In the Supreme Court of the United States

OCTOBER TERM 1995

LELAND COOPER, ET AL., PETITIONERS

v.

MASSACHUSETTS COMMISSIONER OF REVENUE

ON PETITION FOR A WRIT OF CERTIORARI TO THE SUPREME JUDICIAL COURT OF MASSACHUSETTS

BRIEF FOR THE UNITED STATES AS AMICUS CURIAE SUPPORTING PETITIONERS

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QUESTION PRESENTED

Whether state taxation of the non-contributory retirement plan benefits paid to federal military retirees violates 4 U.S.C. 111 when all contributory and some non-contributory retirement plan benefits paid to state and local employees are wholly exempt from state tax.

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INTEREST OF THE UNITED STATES

The Commonwealth of Massachusetts requires members of the United States Armed Forces to pay state income tax on their retirement pay. Pensions and annuities paid to retired state and local government employees, however, are exempt from taxation under the Massachusetts scheme.

The States may not discriminate in taxing the income of federal employees. See 4 U.S.C. 111; *Davis* v. *Michigan Dep't of the Treasury*, 489 U.S. 803 (1989); *Barker* v. *Kansas*, 503 U.S. 594 (1992). The

United States has a continuing interest in ensuring that its employees are not subjected to discriminatory state tax treatment.

STATEMENT

1. Massachusetts imposes an income tax on retirement benefits, pensions and annuities.[1] The State wholly exempts from this tax, however, any "[i]ncome from any contributory annuity, pension, endowment or retirement fund of the United States government or the commonwealth or any political subdivision thereof, * * * to which the employee has contributed." Mass Ann. Laws ch. 62, § 2(a)(2)(E) (Law. Co-op. 1990). Payments received by persons who participated in the pre-1938 noncontributory retirement system for state and local police and firemen are also exempt from the Massachusetts income tax. 1973 Mass. Acts, ch. 876, § 1.

Under the current, contributory retirement system for state and local employees in Massachusetts, 10% of the retirement funds are contributed by the employee and 90% by the government units. *Filios* v. *Commissioner*, 615 N.E.2d 933, 935 (Mass. 1993), cert. denied, 114 S.Ct. 1538 (1994). Massachusetts exempts from the state income tax up to $2,000 per year contributed by an employee to a retirement fund. See Mass. Ann. Laws ch. 32, § 22(10) (Law. Co-op. 1993); *id.* ch. 62, §§ 2(a)(1)(I), § 3B(a)(4). [2]

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[1] Gross income is defined for purposes of the Massachusetts tax as federal gross income subject to state adjustments. Mass. Ann. Laws ch. 62, § 2 (Law. Co-op. 1990). Pension income is included in federal gross income. 26 U.S.C. 61(a)(9) and (11).

[2] The $2,000 limit on the tax deduction for the employee share of the annual contribution is reduced by any amount that the employee has paid that year as his personal share of federal

The Massachusetts provisions have the following effect:

(i) Federal, state and local employees who participate in contributory retirement systems pay no state income tax on amounts contributed by them not in excess of $2,000 per year. Without regard to whether, and to what extent, such personal contributions have or have not in fact been taxed, and to what extent the system is funded by employee contributions, participants in "contributory" plans pay no state tax on retirement benefits as received. (ii) Police and fire employees who receive retirement benefits under the pre-1938 Massachusetts noncontributory retirement system also pay no state tax on their retirement benefits. (iii) But federal military retirees, whose pension system is noncontributory, *do* pay state income tax on retirement payments.

2. Petitioners are Massachusetts residents who paid state income taxes on federal military pension income from 1986 through 1992 (Pet. App. A4). Petitioners filed applications for abatement of the state income tax paid on their military retirement benefits with the Massachusetts Appellate Tax Board, asserting that the more favorable tax treatment afforded to the retirement benefits of state and local government employees violated the nondiscrimination requirement of 4 U.S.C. 111 and the constitutional doctrine of intergovernmental immunity (Pet. App. A4). Relying on the holding of the Massachusetts Supreme Judicial Court in *Filios* v. *Commissioner of Revenue*, *supra*, the Board rejected petitioners' claims (Pet. App. A4).

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employment taxes. Mass. Ann. Laws ch. 62, § 3B(a)(3) and (4) (Law. Co-op. 1990).

3. The Supreme Judicial Court affirmed (Pet. App. A3-A8). Noting that the retirement systems of the Commonwealth and its local governments were "contributory" and that the retirement system of the federal military was "noncontributory," the court concluded that this "determining factor" justified a different tax treatment of the retirement benefits under the plans (*id.* at A5). The court stated that the fact that Massachusetts employees contribute only 10% of the funding of the retirement benefits in their "contributory" plans does not render such contributions "illusory" (*id.* at A7). The court also concluded that the Massachusetts exemption for retirement benefits received by municipal fire and police personnel under the pre-1938 noncontributory system is not "discriminatory within the meaning of 4 U.S.C. § 111" because the exemption favors a class of retirees " 'not because * * * the source of the pay or compensation' is the Commonwealth rather than the Federal government, but on the basis of occupation (police and firefighters) and date of first employment (before 1938)" (*id.* at A8).

ARGUMENT

This decision in this case misinterprets and misapplies the decisions of this Court in *Barker* v. *Kansas*, 503 U.S. 594 (1992), and *Davis* v. *Michigan Dep't of the Treasury*, 489 U.S. 803 (1989). [3]

1. Congress has consented to state taxation of federal employees only when "the taxation does not discriminate against the * * * employee because of

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[3] *Barker* and *Davis* apply to all open tax years and are therefore applicable to this case. See *Harper* v. *Virginia Dep't of Taxation*, 509 U.S. 86 (1993). See also *Reich* v. *Collins*, 115 S.Ct. 547 (1994).

the source of the pay or compensation." 4 U.S.C. 111. This statutory nondiscrimination requirement is coextensive with the prohibition against discriminatory taxes embodied in the constitutional doctrine of intergovernmental tax immunity. *Davis* v. *Michigan Dep't of the Treasury*, 489 U.S. at 812-813. As the Court emphasized in *Davis*, the standard for determining whether a state tax abridges the immunities of the federal government is quite different from the standard under which state economic regulations are tested under the Equal Protection Clause. 489 U.S. at 816. Inconsistent state tax treatment of federal and state employees is permitted only when it "is directly related to, and justified by, 'significant differences between the two classes.'" *Ibid.*, quoting *Phillips Chemical Co.* v. *Dumas Independent School District*, 361 U.S. 376, 383 (1960). Applying this standard, the Court rejected as insufficient the distinctions asserted to exist between federal and state retirement programs in invalidating state tax provisions that discriminated against federal pension benefits in *Davis* and *Barker*.

In this case, Massachusetts asserts a distinction that was not directly at issue in *Davis* or *Barker*. Massachusetts taxes "noncontributory" federal military retirement benefits while exempting from tax the "contributory" retirement benefits paid to other government employees.[4] The Massachusetts

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[4] In *Barker* v. *Kansas*, the Kansas Supreme Court had noted that the military retirement system was noncontributory while the State used a contributory system. See 503 U.S. at 605 n.5. The Kansas court, however, "did not rest its decision on this difference" and this Court therefore did not directly address that issue on the merits. *Ibid.*

court reasoned that the difference between "contributory" and "noncontributory" systems is significant because the Commonwealth taxes personal contributions to the retirement system as income in the year in which the contribution is made. Under the noncontributory federal military retirement system, by contrast, pension funding is not included in the gross income of the employee and is therefore not subject to tax at the time of funding (Pet. App. A6).

This asserted distinction is unpersuasive. Massachusetts retirement benefits are principally funded through government contributions. See, *e.g.*, Mass. Ann. Laws ch. 32, §§ 1, 12(2), 22, 22C (Law. Co-op. 1993). The state or local governmental unit contributes 90% of the funding for retirement benefits; and the state and local employee is not subject to state tax on up to $2,000 per year for any funding that they contribute. See Mass. Ann. Laws ch. 62, §§ 2(a)(1)(I), 3B(a)(4) (Law. Co-op. 1990); note 2, *supra*. Thus, Massachusetts seeks to justify taxation of the *full* measure of military retired pay on the ground that some very small *part* of the benefits received by state and local employees may have previously been taxed by the State (Pet. App. A7).

The rationale of the court below is further undermined by the fact that the Commonwealth exempts from state tax all retirement benefits paid to municipal police and firemen under the pre-1938 *non*-contributory retirement plan. While the record of this case does not disclose how many persons currently receive such benefits, that does not alter the fact that the State's "nondiscriminatory" rationale is inconsistent with the State's facially discriminatory legislation.

Moreover, the rationale offered by the Supreme Judicial Court is foreclosed by this Court's decision in *Davis* v. *Michigan Dep't of the Treasury*, *supra*. In *Davis*, the State sought to justify its tax discrimination against federal retirees by contending that the retirement benefits paid to federal employees were, as a general matter, more generous than those paid to state retirees. 489 U.S. at 816-187. The Court rejected that purported justification because "[a] tax exemption truly intended to account for differences in retirement benefits would not discriminate on the basis of the source of those benefits * * *; rather, it would discriminate on the basis of the amount of benefits received by individual retirees." *Id.* at 817. Under this same reasoning, a tax intended to account for prior taxation of retirement funding would not discriminatorily exempt certain benefits based on their source; instead it would apply to retirement benefits generally and exempt benefits only to the extent that they reflect previously taxed contributions.

Under the standard applied by the Court in *Davis* and *Barker*, Massachusetts's facially discriminatory taxation of military retirement benefits lacks any coherent or consistent rationale. It is therefore invalid under 4 U.S.C. 111. If the decision in this case were allowed to stand, it would serve as a guidepost for States seeking to circumvent the clear restrictions imposed by 4 U.S.C. 111 and this Court's decisions.

CONCLUSION

The petition for a writ of certiorari should be granted.

Respectfully submitted.

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